

Two (or more) into one

Richard Hough, a practitioner in pharmacy law, looks at means of combining together to operate an enterprise on a joint basis



“Joint venture” (JV) is a generic term that describes the commercial arrangement between two or more economically independent entities. It has neither specific meaning nor legal standing in English law and the rights and obligations particular to it are dependent upon the legal form that it takes in each set of commercial circumstances.

Generally, JVs are entered into when a project is undertaken that requires commitment, specific expertise or financial resources from another party on a scale beyond those of an individual company, in return for which that party would normally expect an acceptable amount of equity or profits. Another reason for entering into a JV is “ring fencing”, which allows the legal and commercial risk of a new venture to be sheltered away from core business.

Examples of long-term, pharmacy-specific JVs would be collaborations with property developers, local GPs or other pharmacy contractors for the provision of pharmacy services at a purpose-built health centre, or a pharmacy/nursing home collaboration. A more ephemeral JV could be formed when two or more pharmacies collaborate when tendering for the provision of enhanced pharmaceutical services, such as warfarin testing, to their local primary care trust.

Four options

For most JVs there are four options available:

1. Limited liability company (corporate vehicle)
2. Partnership of individuals and/or bodies corporate (unincorporated vehicle)
3. Limited liability partnership (LLP) (corporate vehicle – essentially a hybrid of 1 and 2)
4. Consortium/co-operation agreement (unincorporated vehicle — contractual agreement).

Very broadly, the four options reflect varying degrees of integration of the JV parties' interests.

The corporate model, typically, involves the vesting of all trading activities, assets and liabilities relating to the JV in a single limited company or an LLP. For ventures in which a number of sole traders actively participate, the LLP may be the most appropriate form. At the other end of the scale, the contractual agreement may involve a negligible amount of integration between the parties, the scale of the project may be small or the duration of collaboration may be short. In some respects, the partnership represents the mid-point between the two other structures. Other factors

which may influence the choice of the JV vehicle are tax, the parties' commercial and financial objectives and location.

Limited company or LLP — Most JVs tend to adopt the corporate vehicle, the numerous advantages of which include that it:

- is a universally recognised medium with a strong identity for third party dealings
- can own and deal in assets
- can sue (and be sued)
- can contract in its own right
- allows the participants to limit their liability and losses
- affords the flexibility to raise finance
- will survive as the same entity despite a change in its share ownership
- allows for a transparent management and employee structure.

The downside to adopting the corporate model is the formality of the structure and the degree of public scrutiny which arises from the regular requirements to file accounts and other information.

Partnership — Whether or not a partnership exists between JV participants is a mixed question of fact and law. A partnership is defined as the “relationship which subsists between persons carrying on a business in common with a view of profit” (Section 1, Partnership Act 1890). This definition, and the resulting statutory obligations, of which the most onerous is that of potentially unlimited liability, will apply to any applicable JV arrangement, irrespective of the parties' express intentions or any explicit, contrary, contractual wording. It is also worth bearing in mind that a partner is liable for the acts and defaults of the other partners.

Consortium/co-operation agreement — The simplest form of JV is a contractual arrangement under which the participants agree to associate as independent contractors, rather than as shareholders in a company or partners in a legal partnership. This vehicle is most suitable where the participants wish to avoid the formality and permanence of a corporate vehicle.

Documentation

The following documentation is usually adopted to establish the basic rights, obligations and objectives of the JV

participants and the procedures involved for when difficulties occur:

- Memorandum and articles of association and shareholders' agreement (for corporate vehicles)
- Partnership deed (for partnerships)
- Membership agreement (for LLPs)

- Joint venture agreement (JVA) (for contractual arrangements)

The rights and duties of the participants, as between themselves and third parties, will, depending on the JV vehicle adopted, derive from the provisions of a JVA or shareholders' agreement and a combination of statutory and common law rules.

Matters commonly dealt with within the documentation would be:

Object and scope — what is the JV attempting to achieve? How long will it last?

Capitalisation and financing — what are the initial and future funding arrangements? How will existing and future financial requirements and tax considerations influence these?

Management — what will be the composition of the board and the directors' responsibilities? Will they, or should they, reflect equity ownership? How will they be remunerated?

Entitlement to profits/assets — how will the profits (and losses) be divided and what mechanisms are in place for deciding to what extent the profits are either reinvested or withdrawn?

Risk-sharing and liabilities — are all risks to be shared by the JV or are some risks to be assumed direct by the participants?

Share transfer — should the free transfer of shares be restricted so that an initial JV participant is not forced to work with an incompatible, incoming party?

Sale/exit procedures — “drag along” provisions in which the sale of a majority shareholding triggers the compulsory acquisition of the minority shareholding at the same share price, and “tag along” provisions in which a minority shareholder can block the sale of a majority shareholding unless a like offering has been made for the minority shareholding.

Minority shareholders — will there be any minority shareholders? How, if at all, will they be protected?

Decision-making — how will a deadlock situation be resolved? Clauses vary from simple procedures such as chairman's casting vote to more obscure mechanisms such as “Russian Roulette” or “Texas Shootout”.

Sickness — how will the JV deal with a participant's absence, failure to participate and ill health?

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Termination — what events will terminate the JV?

Restrictive covenants — how can any participant leaving the JV be prevented from setting up a competing business or from taking its trade secrets, employees or contracts?

Tax — how will the JV be taxed? How will the interests of each participant be taxed?

Employment — what are the rights of those employees transferred from a JV participant to the JV company?

Intellectual property — what might happen to any JV generated IP upon dissolution or a participant leaving the JV?

Warranties — the participants may initially

transfer assets to the JV company in exchange for shareholdings in it, in which case the other participants would wish to obtain suitable warranties or indemnities in relation to those assets.

A well drafted JVA will also commonly contain an express declaration that the participants do not intend to create a legal partnership, but such a statement, while helpful, is not conclusive and would not prevent unlimited statutory liability from arising under partnership law if, on a proper analysis, a legal partnership exists.

So, perhaps the best advice, as in life, is before you leap into bed with someone, take your time to get to know them first. It helps if

you know what you're doing once you get there and if you don't, take direction from someone who does. And if, despite your best efforts, you end up heading for a messy divorce, make sure you've got a good lawyer!

This guide is provided to give an overview of the principal areas when considering JVs and is not a substitute for obtaining detailed legal advice.

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